

the mortgagee obtains coverage for itself as well as the borrower; the NFIP insurance policy is a dual interest policy, whereby one contract covers both the borrower and the lender.

The NFIP *Flood Insurance Manual* should be consulted for additional information about using the MPPP to force place policies.

#### **(4) Conventional NFIP Policy**

A lender also may force place flood insurance by purchasing a Standard Flood Insurance Policy from either a WYO insurer or the NFIP direct program.

If a lender opts to obtain coverage under a Standard Flood Insurance Policy, certain underwriting information must be available to the agent in order to place the policy. If adequate information is available, the rates used to calculate the premium will be the same as used on the Standard Flood Insurance Policy rather than those used under the MPPP.

After the expiration of the 45-day waiting period, if the lender has sufficient information to produce a policy, it may place a policy with an insurer through an agent of its choice. This method of insuring the risk does not entail the use of any specific notice to the borrower.

#### **(5) Private Flood Insurance**

A lender has the option of force placing flood insurance through a private (non-WYO) insurer. Although very few carriers are generally willing to accept personal lines flood risks, some insurers will selectively write the coverage. If private insurance is available, the lender also must consider whether the policy, as well as the insurer, is acceptable to its regulator by meeting the criteria defined by the FIA.

The FIA criteria are fully described in Section E.5 of these guidelines.

### **i. Exceptions**

#### **(1) State-Owned Property**

If the security property is state-owned and covered by adequate policies of self-insurance, flood insurance is not required. FEMA maintains a list of states with adequate self-insurance programs. This exemption, by its terms, applies only to state-owned property, and not county- or city-owned property.

#### **(2) Small Loan**

Section 4012a(c)(2) provides an exemption from the mandatory purchase requirements for any loan made with an *original* outstanding principal balance of \$5,000 or less, and with a repayment term of 1 year or less. The dual criteria must be met in order for this exemption to apply. There is no exemption for home equity or second mortgage loans unless they meet these exceptions.

### **D. CONDOMINIUMS, COOPERATIVES, AND TIMESHARES**

The mandatory purchase requirements apply with equal force to condominium, cooperative, and timeshare units. Placing and monitoring coverage on units within a multi-unit structure present special circumstances to lenders and merit particular treatment. Generally, the applicability of the mandatory purchase law can be explained through a review of how the various NFIP policies correspond to the forms of ownership of common interest community organizations, as follows:

- The RCBAP applies to all high-rise and low-rise residential condominium

## Mandatory Purchase of Flood Insurance Guidelines

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buildings and some timeshares in the Regular Program.

- The General Property Policy applies to cooperatives and some timeshares and condominium buildings not eligible for the RCBAP.
- The Dwelling policy may be issued on an individual unit.

For eligibility requirements and limits available on the various coverages under these policies, refer to the Condominium section of the *Flood Insurance Manual*. Also, see Appendix 10 for the NFIP's Policy Issuance regarding this coverage.

### 1. Condominium Associations

Condominium association board members have a fiduciary responsibility to unit owners to protect the common property by assuring that appropriate insurance coverage is in place. This responsibility includes providing adequate flood insurance to protect buildings located in Special Flood Hazard Areas (SFHAs). A residential condominium association may purchase NFIP insurance coverage on a residential building under the Residential Condominium Building Association Policy (RCBAP). The premium for the policy is usually assessed as part of the unit owner's association dues. A condominium association may opt to purchase flood coverage under the RCBAP, even though individual owners may not have mortgages on their units.

#### a. Residential Condominium Building Association Policy (RCBAP)

The RCBAP is the policy specifically designed for condominiums. Under the RCBAP, the association is able to manage flood insurance needs and by-law requirements without relying on the actions of the unit owners. The valuation of the

property subject to coverage is determined in accordance with Section C.2 of these guidelines.

The Federal mandatory purchase laws apply with equal force to condominium unit owners and their lenders, but the practice of the lending industry, as followed under the RCBAP, is to defer to the association to ensure compliance. A properly placed RCBAP is deemed to satisfy the Reform Act's escrow requirement. Although the association does not bear mortgage responsibility on the individual units, its interest springs from the obligation to maintain and repair the premises for the community benefit and unit owners as tenants in common. A key feature of the condominium insurance format is the separate ownership and mortgaging of individual units, yet the insuring of the structure as a whole is with a policy issued to the association only. Since the RCBAP provides flood insurance coverage protection for both the unit and the common elements of common buildings, the security interests of individual unit owner mortgagees should be protected, so long as coverage amounts reflect insurance to value, as with other forms of property insurance.

The RCBAP directly protects an individual unit owner to the extent that the unit owner has a percentage interest in the property the association owns or maintains. A unit owner's mortgage lender has no direct interest in an RCBAP and is not to be named an additional named insured.

#### (1) Evidence of Compliance

Upon the making, increasing, extending, or renewing of a loan on the unit and as frequently as required, a unit owner and the insurance agent should advise the unit's mortgagee of the RCBAP's existence to ensure that a mortgagee is aware that the mandated insurance requirement is being met.

The unit owner or the producer may provide the mortgagee evidence of the RCBAP by supplying a copy of the declarations page documenting the specific dollar amount of coverage. If a unit owner's mortgagee determines that the coverage purchased under the RCBAP is insufficient to meet the mandatory purchase requirements, it can request the borrower to ask the association to carry adequate limits, or require purchase of a separate unit owner's building coverage policy.

### **(2) Coverage**

Under an RCBAP, the entire building is covered under one policy, including both common and individually owned building elements within the unit, improvements within the unit, and personal property owned in common if contents coverage is carried. The RCBAP does not protect the individual owner from loss to personal property owned exclusively by the unit owner.

The NFIP prohibits duplication of NFIP policies on the same risk. As described below, both an association and a unit owner may obtain NFIP coverage, but the unit owner's coverage is proscribed in that it is in excess of the association policy. The RCBAP is primary in relation to the unit owner's policy.

### **(3) Policy Limits**

The maximum amount of building coverage that can be purchased on a high-rise or low-rise condominium under the RCBAP is the replacement cost value of the building or the total number of units in the condominium building times \$250,000, whichever is less. The maximum allowable contents coverage is the actual cash value of the commonly

owned contents up to a maximum of \$100,000 per building.

### **(4) Coinsurance Provision**

The RCBAP encourages an association to purchase coverage in an amount equal to at least 80 percent of the replacement cost of the structure or to the maximum amount of coverage available under the NFIP, in order to avoid the coinsurance penalty. If that threshold is met, the NFIP agrees to pay 100 percent of all compensable partial losses up to the limits of the policy minus any deductible. When an association carries limits to full replacement cost value, the unit owner does not need to obtain supplemental structure coverage to cover a potential assessment in a total loss situation. The RCBAP's coinsurance provision requires a condominium association to carry NFIP coverage exclusively to comply with the insurance-to-value provisions.

Lenders must be aware of the coinsurance clause that applies if the association has not obtained appropriate coverage. To the extent the association has not purchased NFIP coverage in an amount equal to the lesser of 80 percent or more of the full replacement cost of the building at the time of loss, or the maximum amount of insurance available under the NFIP, the insured will not be reimbursed fully for a loss. Building coverage purchased under individual dwelling policies cannot be added to RCBAP coverage in order to realize the 80-percent requirement. The amount of loss in such a situation will be determined in accordance with the policy's coinsurance formula.

### **b. Dwelling Policy**

A unit owner can acquire supplemental building coverage to the RCBAP by purchasing a unit policy under a Dwelling

Policy form that is written in excess of the association policy. The policies are coordinated such that the Dwelling Policy purchased by the unit owner responds to shortfalls on building coverages pertaining either to improvements owned by the insured or to assessments.

Assessment coverage, which is available under the unit Dwelling Policy, applies when the building covered by the RCBAP is insured to 80 percent of replacement cost. The assessment coverage under the Dwelling Policy form will respond only when a loss exceeds 80 percent of replacement.

This assessment coverage also applies to common elements of any other insured building of the condominium association insured to value in the name of the condominium.

Personal property owned by individual unit owners must be insured under an individual unit owner's Dwelling Policy.

### **c. General Property Policy**

A condominium association may purchase coverage under the NFIP on a nonresidential condominium building under this policy. Both building and contents coverages are available separately, in amounts up to \$500,000 per nonresidential building.

The nonresidential unit owner is required to purchase contents coverage using the General Property Policy form.

## **2. Cooperative Associations**

The NFIP offers coverage for cooperatives through the General Property Policy form, with a maximum amount of building coverage up to \$250,000 available to a residential cooperative. The entity that owns the cooperative, not the various unit

members, is the named insured. A cooperative cannot be insured under the RCBAP.

## **3. Timeshares**

NFIP coverage of timeshares is directly related to the jurisdiction's property ownership rights, as influenced by state law. The jurisdictions generally can be divided into two categories:

- Fee or real-estate ownership
- Non-fee interest, such as right-to-use.

States with fee ownership number slightly more than half of the jurisdictions.

In a fee-ownership jurisdiction, a timeshare is considered similar to a condominium. Therefore, the RCBAP is the required policy form for residential timeshares if the risk otherwise meets the underwriting requirements. That is, a timeshare unit owner must hold an interest similar to that of a condominium unit owner to be eligible for coverage under the RCBAP. If a timeshare is eligible for an RCBAP, it is precluded from being insured under a General Property Policy. A fee-ownership timeshare requires coverage placed through the timeshare's association on the RCBAP form. A single 52-week block of timeshare ownership is considered as a single interest, rather than as separate interests per timeshare owner. As with a condominium, lenders may consider the RCBAP policy, with the association as the named insured, as complying with the mandatory purchase requirements.

In a non-fee jurisdiction, the title remains with the building owner who has the full insurable interest in the real property, not with the unit occupants. In this situation, a General Property Policy form must be used on the structure. The non-fee simple form of ownership is very similar to a cooperative, where no deed is held by the unit owner.

### 4. Secondary Market

In their selling guides for purchase of mortgages on condominium units, Fannie Mae and Freddie Mac specifically address the requirement of property coverage. These Government-Sponsored Enterprises also recognize flood coverage carried by the association as complying with the mandatory purchase requirements.

#### a. Fannie Mae

Fannie Mae will accept structure coverage provided under a Dwelling Policy form to supplement inadequate coverage carried by an association if the association carries 80 percent of replacement cost coverage on the condominium. If a condominium association declines to carry any flood coverage, then each unit owner may purchase an individual policy to comply with Fannie Mae's requirements. The Fannie Mae guide also states that unless a higher maximum deductible amount is required by state law, the maximum allowable deductible is the higher of \$1,000 or 1 percent of the face amount of the policy.

#### b. Freddie Mac

Freddie Mac's guidelines are more restrictive than those required by the statute; it will not purchase loans on condominium units unless the association insures to full replacement value of all improvements. The policy deductible cannot exceed the higher of \$1,000 or 1 percent of the policy's insurance limits.

### E. KEY PROVISIONS

The preceding sections of these guidelines discuss specific provisions of the Act and regulations as they apply to an individual borrower or policyholder. This section describes how certain key provisions of the

Act are to be implemented within the lending industry.

### 1. Tripwires

#### a. Loan Activity

As stated in the Congressional committee report, Congress views the making, increasing, extending, or renewing of a loan as a "tripwire" for compliance with the flood insurance purchase requirements. This tripwire occurs most frequently upon loan origination, e.g., when a lender knows or has reason to know whether the mandatory purchase requirements apply. Another trigger involves any situation that alerts a lender or servicer to a change in circumstances, e.g., a known map change, or the receipt of a notice to pay the premium to avoid policy expiration.

If a borrower executes a note on improved real estate as collateral for a personal loan, and the lender does not perfect a security interest or mortgage in the structure itself, the loan is not a "designated loan" and, therefore, is not subject to the mandatory purchase requirement.

#### b. Loan Transfer or Purchase

The transfer or purchase of a loan among regulated lenders or servicers does not constitute the making of a loan, so it does not trigger the mandatory purchase requirement.

It is the lending regulators' position that deeming a loan purchase as a regulatory tripwire could result in the imposition of duplicative and potentially inconsistent requirements on the seller and purchaser of loans sold in the secondary market. As a condition of purchase, a loan purchaser may require the seller to determine whether the property securing the loan is in a Special